

## **Industry Sector Analysis**

### **The Danish Financial Services Sector**

#### **Summary**

A wide range of sources of finance exists in Denmark, from public incentives and private investors to banks, venture capitalists and institutional investors. The choice of financing will depend on the company and its focus of business activities, the management, the stage of development of the company, the amount of capital needed, etc.

Total assets in the commercial and savings-bank sector amounted to DKK 28.2 billion (USD 4.40 billion) in 2004. The Danish banking sector comprised 198 banks, operating 2,014 branches (excluding branches of foreign banks). Commercial and savings banks accounted for 37% of the overall financial sector balance, with mortgage credit institutions representing 31%, and insurance companies and pension funds accounting for 28%. The remaining 4% is made up of stockbrokers and investment trusts.

Electronic banking is common practice in Denmark. Functionality varies, but it generally exceeds the European average. There is no bank-independent electronic banking standard in Denmark. Many proprietary systems allow corporate users to manage both their bank accounts and payment transactions. Internet banking is becoming increasingly commonplace among retail users and small companies.

#### **Background**

The high economic growth until the first oil crisis brought about a sizeable increase in activity in the financial sector, while liberalization of the financial markets and the significance of technological developments for the supply of financial products created fertile ground for a particularly strong increase in employment in the second half of the 1980s. The end of the 1980s was characterized by a clear tendency towards concentration in Danish business life in the form of takeovers and mergers, which for their part created a need for larger and financially stronger Danish financial institutions. So during these years the financial sector experienced a period of mergers and acquisitions which, broadly speaking, halved the number of financial institutions and saw the establishment of the two major banks, Den Danske Bank and Unibank.

The potential for rationalization in the wake of the period of mergers, together with deteriorating results in the sector, led to a considerable adjustment of the financial institutions' balances and operations between 1992 and 1993. Among other things, this has resulted in a better balance between deposits and loans, a reduction in the number of domestic branches by a third, and a reduction in the number of employees by 25% between 1989 and 2000. Although this has considerably reduced total costs, the Danish banking sector continues to be too labor intensive in an international perspective. An attempt has been made to improve profits in the financial institutions through greater use of bank charges. Furthermore, the financial institutions have benefited from the technological development and the concept of e-banking has expanded substantially since the late 1990s.

The creation of the EMU in 1999 caused a new wave of European mergers which did not spare Denmark. Unibank decided to take part in a Nordic co-operation, while Danske Bank merged with Danish institutions. Thus, Unibank merged with the Swedish-Finnish Bank MeritaNordbanken in March 2000, and in November that same year the Norwegian bank Christiania Bank og Kreditkasse joined the group which changed its name to Nordea shortly after. Nordea is clearly the leading financial institution in the Nordic countries. In October 2000 Danske Bank merged with RealDanmark (BG Bank and Realkredit Danmark) to form the largest Danish financial institution.

In common with the international trend, compound trading had started in Denmark leading in the direction of so-called financial supermarkets, which were able to offer all forms of financial services. Thus both Danske Bank and Unibank built up their own mortgage lending institutions and pension funds at the beginning of the 1990s, while existing mortgage lenders and insurance companies on the other hand began to offer traditional banking services, e.g. borrowing and lending.

Internationalization had moreover meant that Danish financial companies had already established themselves abroad in the 1980s with representative offices, branches or subsidiaries. On the other hand, they experienced increasing foreign competition in the domestic market.

The generally sharper competition together with unfavorable market conditions from 1987 to 1993 led to losses amounting to billions of kroner in the financial sector. The resulting losses and debt provisions amounted to approx. 2.5% of total outstanding loans and guarantees 1992- 1993, which was high, though not without precedence. This was gradually improved, following the economic upswing, which began around 1993. In 2000, losses and debt provisions amounted to less than 0.3% of total loans and guarantees.

### **Competitive Analysis**

Compared with other countries Denmark has always had a very high concentration of banks. The two largest commercial banks in Denmark are Danske Bank and Nordea. With two thirds of the market, these two banks are a dominant force in the banking sector. However smaller banks still continue to flourish, many of them are based entirely on local and regional business.

The Danish banking market today consists of approximately 90 banks operating approximately 2,000 branches. The total includes five branches or subsidiaries of foreign banks, while other foreign banks have established representative offices in Denmark.

The banks' basic dependency on foreign trade means that international transactions and co-operation have always been an integral part of Danish banking. Parallel with growing Danish exports and increasing economic interaction with foreign countries, the banking sector has expanded its international involvement.

The larger banks have set up offices in the main international banking centers like London, New York, Singapore and Tokyo, and smaller banks operate through correspondent banks in these and other centers.

Internationally, the most prominent sector in Danish financial services is the Danish bond market, which is generally rated the seventh largest globally, and the fourth largest in Europe. The volume and liquidity of the bond market has attracted a growing volume of new issues from other countries, and made Copenhagen an important center for bond trading.

Bonds, shares and derivatives - futures and options - are all traded through the Copenhagen Stock Exchange. This exchange pioneered computerized trading internationally, and was the first to introduce electronic bonds and shares, administered by the Danish Securities Centre where all transactions and documentation of ownership are recorded.

Generally the Danish banking sector is a high-tech industry, and the services, which it is able to render customers nationally and internationally, reflect this. The banks have invested heavily in computer systems to achieve higher productivity. The efficiency of the sector is reflected in the highly sophisticated and efficient money transmission systems based on various types of credit cards and a nation-wide electronic payment card system (Dankort).

The market is characterized by heavy competition and furthermore interest rates are at their lowest levels for decades, and prospects for obtaining business-related loans are currently excellent.

There are about 161 non-life insurance companies operating in Denmark, 70 limited companies, 82 mutuals and 9 foreign companies. Premium incomes after deduction of reinsurances amount to about DKK 30 billion (USD 48 billion) yearly.

## **Statistical Data**

### **Largest Banks in Denmark**

<b>Million USD</b>	<b>Working capital</b>		<b>Deposit</b>	<b>Loans</b>		<b>Balance</b>	<b>Employees</b>
Danske Bank	126,204	80,971	84,329	229,319			16,537
Nordea Bank	40,208	35,391	31,753	78,369			7,436
Jyske Bank	14,242	10,442	9,126	20,558			3,713
FIH	8,737	246	8,556	10,630			2,075
Sydbank	8,563	7,213	7,911	13,036			165
Spar Nord	3,973	3,424	3,189	6,046			1,103
Nykredit Bank	3,930	3,217	3,769	12,287			362
Arbejdernes Landsbank	2,181	1,859	1,331	2,939			973
Forstædernes Bank	1,893	1,546	1,955	2,878			461
Alm. Brand Bank	1,707	1,531	1,492	2,356			278
Fionibank	1,701	1,401	1,706	3,237			513
Amagerbanken	168	1,385	1,384	2,227			483

Sparbank Vest	1,396	1,194	1,230	1,565	503
Roskilde Bank	1,372	1,065	1,625	2,151	404
Danske Andelskasser	1,285	1,089	897	1,346	536
SEB	1,261	466	1,272	1,325	51
Lån og Spar Bank	1,161	1,054	551	1,270	311
Sparekassen Kronjylland	1,090	861	696	1,330	359
Ringkjøbing Landbobank	1,064	857	1,197	1,584	253
Nørresundby Bank	885	754	606	977	270
Sparekassen Sjælland	815	622	574	911	211
Nordjyske Bank	749	637	454	808	252
Din Bank (SkandiaBanken)	640	591	351	665	234
Sparekassen Lolland	630	483	494	754	166
Sparekassen Himmerland	609	458	430	682	160
Morsø Sparekasse	598	468	449	669	103

Source: The Danish Bankers Association, 2004

### **End-user analysis & Financial Characteristics**

A wide range of sources of finance exists in Denmark. From public incentives and private investors to banks, venture capitalists and institutional investors, many choices of financial services are available to the end-users.

The Danish banking system is very efficient and has a good IT infrastructure making it easy and fast to open an account for users. A wide range of financing options is available to companies' day-to-day operations and fixed asset investments. In addition to ordinary banking transactions, the banks also offer financial services such as insurance, mortgage financing, real estate services, asset management and leasing.

Danish banks are far ahead in electronic cash management. The banks have developed electronic banking systems that may be adjusted to the individual needs of companies, including integration with financial management systems. The banking systems can handle accounts with banks in other countries, control cash flows and make it possible to retrieve information and manage liquidity efficiently both in and outside Denmark.

#### **Credit transfers**

Credit transfers are the most widely used payment instrument for commercial payments e.g. pensions, salaries, business-to-business payments and social security benefits. Usage has increased substantially over the last decade. Paper-based credit transfers are widely used for non-recurring retail payments, but are increasingly being replaced by electronic credit transfers.

#### **Direct debits**

Operated by PBS (Danish Payment Systems Ltd), the BetalingsService (direct debit service) is used by the vast majority of households to pay their bills. The debtor receives a monthly summary showing what will be paid to whom – and when – during the coming month. PBS also operates a pre-authorized direct debit system, known as the

LeverandørService (supplier service), for corporate customers. Upon prior agreement with the customer, suppliers draw amounts directly from the customer's bank account.

### Checks

Payments by check have more than halved in volume in the last ten years due to the increase in usage of credit transfers, direct debits and card payments. The average check transaction value has increased since 1991, which indicates that the reduction in check usage has primarily taken place in personal transactions. All checks are truncated.

### Card payments

PBS administers the national debit card, Dankort, the most commonly used payment instrument in Denmark. The Dankort card can be used as a debit card via terminal or paper-based systems and as a cash withdrawal card. The Dankort is currently based on magnetic strip technology but there are plans to introduce chip cards. Combined Dankort/Visa cards are becoming increasingly popular, enabling Danes to pay for goods and withdraw cash abroad. PBS also administers the Danmønt stored value card. The Danmønt card is a chip card used in places such as parking meters and station ticket machines. It is available in two versions: disposable or rechargeable.

### Notional pooling

Notional pooling is permitted between both resident and non-resident accounts as well as different legal entities. However, the Danish banking authorities do not allow credit institutions to offset notionally pooled credit and debit balances. Consequently, notional pooling is costly and not widely offered by domestic banks. Instead, some banks have developed interest rate enhancement solutions offering interest compensation cross-border and cross-currency. These products are mainly aimed at the Nordic marketplace.

### Cash concentration

Cash concentration is also permitted between resident and non-resident companies. However, there are restrictions on inter-company lending to parent companies outside the European Union. Most companies prefer to manage their liquidity via cash concentration (in particular, zero- and target-balancing). Another cash concentration technique that is widely used is single legal account pooling (also known as balance netting) whereby only one account acts as the master account and the other accounts are merely memo accounts.

### **Characteristics of the Danish bond market**

Seen in an international perspective, the Danish bond market has a considerable volume. The Danish bond market is one of the biggest in the world and the volume of all bonds in circulation totaled around DKK 2,500 billion (USD 400 billion) at the end of 2003.

Mortgage bonds amounted to around 69% of all bonds in circulation.

The Realkreditrådet was set up in 1972 and functions as the trade organization for all mortgage banks in Denmark. At present there are eight mortgage banks in Denmark that grant mortgage credit loans:

- BRFkredit concentrates its lending activities on owner-occupied homes, including weekend cottages, subsidized and private rental homes, office and shop premises and certain types of industrial properties.
- DLR Kredit grants loans to agricultural, horticultural and forestry properties etc to non-profit and private homes for rent, private co-operative housing societies and to office and shop properties.
- FIH Realkredit, FIH Realkredit, which is a subsidiary of FIH Erhvervsbank, has so far been concentrating its activities in the areas of manufacturing and manual industries etc., but stopped granting new loans in 2004.
- LR Realkredit mainly grants loans to large construction projects, primarily publicly subsidized projects.
- Nordea Kredit is part of the Nordea Group and grants loans to all property categories except for some types of publicly subsidized building projects.
- Nykredit Realkredit will grant loans to all property categories.
- Realkredit Danmark is part of the Danske Bank Group and grants loans to all property categories.
- Totalkredit, which is a fully owned subsidiary of Nykredit, grants loans to owner-occupied homes and weekend cottages.

All mortgage banks operate on a nation-wide scale, and some of the mortgage banks have made use of the possibility of granting loans abroad.

### **Further Information**

For further information about the Danish Financial Services market, please contact CS Copenhagen.

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